Chapter 2

LITERATURE REVIEW

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Preceding chapter explains the concise idea of microfinance and presents the outline of the study includes rationale of the study, objectives of the study, organization of the thesis and contribution of the study. This chapter discusses the reviews regarding the social aspects and financial aspects of the microfinance reviewed by the Indian authors in addition to foreign authors.

As part of this research work, the researcher undertook a review of literature on microfinance on social and financial aspects. Microfinance is a significant tool for poverty alleviation. Microfinance institutions provide all types of financial facilities to the poor but among all financial facilities most important facility is micro credit to the poor without any collateral. Therefore, most challenging area for microfinance providers is repayment. The researcher specially focused on repayment capacity of microfinance borrowers. This chapter highlights the contributions made by various experts and scholars in the field of microfinance.

The chapter divided into following sections: section 2.1 covers the reviews of contributions by Indian authors and section 2.2 covers the reviews of contributions by foreign authors.

2.1 Reviews from Indian Authors

Many Indian authors have contributed their significant views in the field of microfinance. Some of the reviews has been included here as a part of the research.

2.1.1 Social Aspects

M. Anjuman and T. Alagumani[1] (2001) studied that whether the SHGs, formed by NGOs, really cater to the needs of the people in the rural areas or not? Mariamman kalangiam, the SHG located at Kodikulam village in Madurai district was selected as a sample and required information was collected by personal interview method during the period of 1997-98 to 2000-01. The purposes of the loan given by the SHG were house repairing, social obligations, medical expenses, buying assets, electricity connection, purchase of livestock, etc. The SHG helped the members to use the loan properly which resulted in 100 per cent repayment. It had increased the awareness of members for girls' education, improved outside contact and decision making skill. This case study has clearly indicated that if the group formation was correct, this would have positive impact on all aspects.

Rekha R. Gaonkar[2] **(2001)** studied the working and the impact of Self-Help Groups (SHGs) based on data collected from five women's SHGs situated in Bardez and Bicholim talukas of Goa. The study revealed that individual loans were mostly used for productive purposes with monthly interest rate 2 to 3 per cent and recovery rate was cent per cent. In the group system decisions were to be taken after frank group discussion. Proper financial records were to be maintained by the groups. Thus, SHGs had made a lasting impact on the lives of the poor, particularly women. The quality of life of the poor had improved a lot. The paper concluded that the movement of SHGs could significantly contribute towards the reduction of poverty and unemployment in the rural sector of the economy. The SHGs could lead to social transformation in terms of economic development and the social change.

Prema Basargekar[3] **(2010)** has analyzed the meaning and role of social capital with specific reference to microfinance programme and tries to measure its impact on social empowerment of women with the help of empirical findings. Primary data were collected of 217 women Self Help Group (SHG) members by using random sample method from the SHGs organized by Forbes Marshall Co. Ltd, a leading manufacturing company in Pune, Maharashtra, India as an initiative of corporate social responsibility. The study found that microfinance can build social capital to improve the effectiveness of desired outcome such as social empowerment of women. The activities conducted to run microfinance programmes such as conducting monthly or bi-monthly meetings, peer monitoring on individual member's financial transactions, using social network, creating a platform for collective action create social capital. Microfinance has helped creating and sustaining positive social capital where women have benefitted by enhancing their level of consciousness, awareness, decision making abilities and improvement in wellbeing through collective action.

K. Rajendran and R.P.Raya[4] **(2010)** have examined the impact of microfinance on the empowerment in psychological, economic and social aspects and managerial skills of leaders of SHGs and their attitude in Vellore district (Tamil Nadu, India). Natrampali and Nemali blocks in Vellore district were selected for the study since those two blocks have similarities on number of SHGs and poverty level. 45 SHGs in each block were selected randomly, 180 leaders and animators of the groups were interviewed with the pre tested and well structured questionnaire schedule during 2008-09. Statistical tools, both average and percentage analyses were used to draw the influence of variable in each psychological, economic and social aspects and managerial skills improvement. The study found positive impact of microfinance showing improvement in all the aspects. ANOVA test was also used test the significance of blocks on the improvement of each of the three aspects and found that there is significant relationship between the block and the improvements in economic and social aspects, and managerial aspects of respondents. However, the study found no significant influence of the respondents' age and education on the improvements in Psychological, Economical and Social and managerial aspects. The results of the study clearly indicated that microfinance brought social mobility among women.

Naresh Singh[5] (n.d.) made an attempt to understand the growth of microfinance at global level in general and in India in particular and how micro-finance sector can contribute significantly for building social capital. From the review of literature it has been revealed that social system and subsystems of this culture are built on exploitation. The rich are exploiting the poor by putting them into a debt-trap of money-lending system. Microfinance is an intervention based on social intermediation in which poor people can mobilize their savings, link it with credit and finally become self-employed. It resulted in building social capital. The social development approach of microfinance is based on the premise that people should earn money by investing in viable micro-enterprises. They should earn profit from their enterprises. Major share of the profit should be reinvested in enterprises for their growth. The other share of the profit should be spent on social development that is, health, education, housing, sanitation etc. Process of Social intermediation is an investment that is made for development of both human resources and institutional capital to make marginalized groups self-reliant in preparing them to engage in formal financial intermediation.

2.1.2 Financial Aspects

Jayshree Vyas[6] **(1993)** discussed about the need of credit and savings facilities to poor women and their repayment capacities. SEWA Bank has begun to solve women's problem by providing them financial facilities like credit and savings. The bank had only 10% defaulters up to 1985 and 12% up to 1993. Common reasons were sickness, death in family, social customs, delay in payment of wages, husband's unemployment, anti-social influence, sheer stubbornness and vengeance against group leader or organizer etc. The paper concluded that personal and continuous contact with poor women is almost precondition while banking with them which helps the bank to understand the needs in better ways. Integrated approach of providing many supportive services over and above credit is also very important. Close coordination between members, organizers and directors needed to keep the bank's operations flexible and dynamic.

Maitreesh Ghatak[7] **(1999)** analyzed how group lending programs use joint liability to utilize local information that borrowers have about each other's projects through self-selection of group members in the group formation stage. He defined models for two types of credit contracts in this environment: individual-liability contracts and joint-liability contracts. The study concluded that group lending based on joint liability, could raise expected aggregate surplus and could achieve high repayment rates even when borrowers had no conventional collateral to offer, compared to lending based on individual liability because it was based on the fact that borrowers were asked to self-select group members and this leads to differential expected costs of borrowing to borrowers depending on their type because the types of their partners were different from the same joint-liability contract.

Maitreesh Ghatak, Timothy w. Guinnane[8] **(1999)** discussed how joint-liability lending promotes screening, monitoring, state verification and enforcement of repayment and how joint liability works in practice. The study was based on the available empirical literature regarding joint liability lending and/or institutions. The study discussed with two important institutions that have successfully used joint liability: Germany's historical credit cooperatives and the Grameen Bank because these two institutions provide a basic outline of the various ways joint-liability lending can work. The study showed that joint liability can achieve better screening to contend with adverse selection, encourages peer monitoring to reduce moral hazard, gives group members incentives to enforce the repayment of loans, and reduces the lender's audit costs for cases where some group members claim not to be able to repay. The defaulters in the group were excluded from the group and threaten for not disbursing another loan to the group. This threat was less effective in individual lending. In practice there is clear evidence that joint-liability improves repayment, but these institutions use other instruments as well, and no study yet tries to apportion the reasons for success.

In **(2000) Jayshree Vyas**[9] pointed out that banking with the poor can be sustainable. If the poor are served with suitable financial services they can too become good repayers of loans. They are also economically active and can contribute to the national economy. She suggested that banking with the poor needs to be considered as a potential banking business not as a welfare activity.

K. C. Sharma[10] **(2001)** discussed that micro financing is about provisioning of thrift, credit and other financial services and products of very small amounts to the poor in rural semi-urban and urban areas for enabling them to raise their income levels and to improve their living standards. Usually SHGs focus on the poor especially on poor women. More than 85 per cent of the SHGs linked to bank were reported to be women. It was estimated that the outreach of formal financial institutions, *i.e.* commercial banks, co-operative banks and regional rural banks ranged between 30 to 40 per cent of the households in terms of loan account. But in terms of individuals it was much less, and in terms of saving account, this proportion was higher. It was reported that significant changes in the living standards of SHG members have taken place in terms of increase in income levels, assets, savings borrowing capacity and income generating activities. However, caution needs to be exercised to safeguard healthy growth of SHG movement in India.

D. S. Navadkar, K. S. Birari and D. V. Kasar[11] (2001) made an attempt to examine the micro credit funding in India and its progress in Self Help Group bank linkage programme and bank policies in micro credit funding. The study was based on secondary data. The study indicated that National Bank for Agriculture and Rural Development (NABARD) and Rashtriya Mahila Kosh (RMK) are the two important funding agencies for NGOs or SHGs. The NABARD had established good linkage covering 97.52 per cent of the total NGOs or SHGs. However, the RMK had funded 39 percent of the total micro credit sanctioned through all sources. There was a significant progress in SHG linkage programme from 1999-2000. The SHG received loans at the interest rate of 12 per cent per annum directly from the banks or NGOs. The study suggested that the SHG bank linkage should be strengthened to provide micro credit to the rural poor.

G. Srinivasan, S. Vardharaj and M. Chandrakumar[12] (2001) analyzed the comparative financial performance of rural and urban SHGs in Coimbatore district of Tamil Nadu. For the purpose of the study 50 SHGs (25 each from rural and urban area) were selected from the district. The data were concerned about total membership, total lending, total savings, total recovery, total default etc. All information was collected from the offices of selected SHGs during the period of 1999-2000. Results had been found by the following methods *i.e.* recovery index (ratio of total recovery to total lending), thrift credit ratio (ratio of total savings to total lending) and outstanding credit ratio (ratio of total outstanding to total lending). The study indicated that the average total membership, the average total savings, the average total lending and the average total defaults were found to be higher in rural SHGs than in urban SHGs. The rural SHGs showed lower average recovery index and higher average outstanding credit ratio than the urban SHGs because of higher defaults. Only the average thrift credit ratio of urban SHGs was lower than rural SHGs. The study concluded that the overall financial performance of the urban SHGs was better than of the rural SHGs.

K. K. Kundu *et al.*[13] (2001) have collected information about five randomly selected SHGs from Gurgaon district of Haryana. Primary data from the selected SHGs were collected by personal interviews in June 2001. The secondary data were collected from National Bank for Agriculture and Rural Development (Gurgaon) and The Gurgaon Gramin Bank. The paper attempted to study the composition and organizational structure of selected SHGs in the study area and to examine the characteristics/performance and the major constrains inhibiting the sustainability of these SHGs. The study revealed that both formal and informal SHG – bank linkage programme operated in the district with uneven block wise performance. The regional rural bank, *viz.* Gurgaon Gramin bank played an active role in the bank linkage programme so as to improve the access of the rural poor to financial services in a cost effective and sustainable manner, though commercial banks made moderate efforts. Both formal and informal SHGs were formed with homogenous groups of similar socio economic strata and involved in lively discussion with the members for determining their creditworthiness, need and exact requirement, income and repayment possibilities etc. The rural poor developed confidence in them and also cultivated the habit of thrift and utilization of collective wisdom to tackle their own problem through SHGs. It was suggested that if the rural poor were properly organized and given the proper set up, micro financing as a supplementary to the existing rural credit operations would help to ensure increased access to credit for them.

V.K. Ramacharan and Madhura Swaminathan[14] (2001) gave some highlights on dealing with over dues with an Indian example of SEWA Bank. In the financial years 1996-97, 1997-98 and 1998-99, NPAs in SEWA Bank amounted to 28%, 20% and 27% respectively of total loans and advances. For the same period, 1995-96, 1996-97 and 1997-98, the RBI estimates that gross NPAs as a share of the total advances of all public-sector banks together amounted to 17.3%, 18% and 16%. SEWA Bank took measures to address the problem of overdue loans involve greater supervision and monitoring. In short, higher and better repayment requires more staff and closer monitoring.

Asif Dowla and Dewan Alamgir[15] (2003) had presented the paper with the objective that how the microfinance industry in Bangladesh has evolved from its initial focus on credit, disbursing standardized loan products and collecting obligatory savings to the development of flexible savings products. Another objective of the paper was to show that rapid escalation of savings without a proper legal framework can be problematic. By reviewing different literature the study pointed out that the microcredit programme in Bangladesh was fundamentally a savings and credit programme. The regularity of savings and attendance in group meetings were preconditions for receiving credit. MFIs didn't allow withdrawal of compulsory savings for a number of reasons. If a member fails to repay the loan, her savings are adjusted against the outstanding loan. However, some MFIs had relaxed the rules on withdrawals from compulsory saving and provided flexible savings accounts too. Now the only requirement was that a member must deposit regularly for a period of eight weeks to quality to receive credit and his or her savings can be withdrawn any time by any amount. But one legal issue raised regarding saving mobilization was only commercial banks and Grameen bank were allowed to mobilize savings from public while other NGOs/MFIs did not have the legal mandate to collect savings. The cooperative law allowed the MFIs to accept savings from their members only. Collecting savings from non-members was completely a new dimension in financing microcredit program in Bangladesh. But there was no law to protect the deposits of the savers. It was suggested that appropriate regulation must be introduced regarding the following: (1) Every NGO/MFI should not be allowed to introduce all kinds of savings products; (2) the maximum amount of savings that can be mobilized by each type of instruments should be determined; (3) MFIs willing to introduce long-term savings products must maintain superior quality of portfolio, and better internal financial and management discipline.

The objective of **M S Sriram, Smita Parhi**[16] **(2004)** was to understand the financial flows of the rural poor from Alisgarh, the village in Udaipur district, Rajasthan. The primary data was collected by survey method. 36 BPL (Below Poverty Line) families consulted with Seva Mandir, a large NGO working in that area, were selected as a sample. The secondary data included different views of the existing literature. It was observed that the most killing expense was health related which leads the poor into further indebtedness. There were various studies conducted to identify the factors that drag people into the poverty trap, the major findings were the overall asset-saving-income profile of the poor in that village gave comfort while compared to the indebtedness. However, the most of the assets and savings were illiquid, forcing the poor to borrow at high cost and service such loan. This study presented the results of a pilot study, conducted in Alsigarh village, was a precursor to an all-India study.

Sampati Guha and Gautam Gupta[17] **(2005)** had presented the study based upon field level observation of a large Rosca programme in West Bengal facilitated by

JDS (Jeevika Development Society, an NGO in West Bengal). Rosca can be defined as a self-selected, voluntarily formed group of individuals who agree to save and contribute a pre-committed amount of money in every period towards the creation of a fund. This fund is then used to allot fixed amounts to each member in turn in accordance with some pre-arranged principle. Once a member has received the fund, she is excluded from any allotments until the Rosca ends, but must continue to participate in contributing to the fund. Members use this fund for different purposes. From the survey conducted by JDS of 1074 members, it was observed that about 17 per cent of the sample was engaged in income generation activities, majority of whom were following Hinduism and were from general caste. Thus, NGO failed to motivate the larger section of the scheduled caste population to join the Rosca. The loan of ₹500 was repayable in 10 equal monthly instalments. The group charged each member 1 per cent interest per month on reducing balance. It was observed that default rate was as low as 26.7 per cent. The study found that demand for loans arises from three reasons: (i) working capital for production activities, (ii) unforeseen consumption needs and (iii) repayment of previous loan borrowed at high rates of interest. It was pointed out that 12.38 per cent of members belong to the lowest income group *i.e.* ₹0 - ₹500 per month. It can be said that the extremely poor section of the population was not motivated to join the Rosca because it requires the ability to save (albeit a small amount) as well as to repay the loan. JDS model suggested that defaults might be addressed through the use of loan sequencing (raises the monitoring activity among members who receive the fund later, or their peers, who received the fund earlier) and the dissolution fund (members have to save continuously while repaying the loan and the fund is equally shared by continuing members when the group is dissolved, however, defaulting members are excluded from sharing in this fund).

Sriram M. S.[18] **(2005)** had attempted to review the performance of formal institutional channels of microfinance and discussed the emergence of new forms of collaboration in the delivery of microfinance services. It was pointed out that in the case of commercial banks; the percentage of net bank credit deployed in the priority sector was 42 per cent in 2003 – up from 39 percent in 1999. The public sector banks and private sector banks had consistently failed to meet the target to reach weaker sections of the society. The figures of public sector banks indicated that the level of NPAs in the category of weaker section advances was 20 percent in 2003. RRBs (Regional Rural Banks) were created to offer targeted lending in rural areas but their performance over the years had not been very heartening, though the NPA of RRBs declined to ₹16.1

crores (2002) from ₹36.8 crores (1997). The district cooperative banks too did not present a rosy picture on the recovery front. In 2002, the recovery of these banks was 66 per cent. Of a total of 368 district cooperative banks, 258 were showing profits and 110 losses. One of the most successful programmes supported by the state in the microfinance sector has been the bank linkage programme. Around seven lakh groups were linked to the banks and around five lakh groups were refinanced by NABARD by 2003. Under IRDP (Integrated Rural Development Programme) scheme, bank credit to the tune of ₹1,109 crores was disbursed to around eight lakh poor people in 2001-02. It was pointed out that the experience of microfinance indicates that it is possible to have high repayment rates, if credit is dispensed appropriately.

Karuna Krishnaswamy[19] (2007) focused on competition and multiple borrowing in the Indian Microfinance Sector. The study depends upon both primary and secondary data. The study considered the loan and repayment records of over 500,000 clients from seven MFIs. But from all seven MFIs, the incidences of multiple borrowings were identified and those clients were selected as sample for the study. The interviews were conducted only with a small set of clients; the results could not be generalized. All of the women interviewed indicated that they needed more loans to meet their investment needs but they did not have concern about their ability to repay. Loan officers also did not concern about the client's multiple borrowing. They concerned only about getting their weekly payments. It was observed that though multiple borrowing help majority of the clients, some of the clients would get deeper into debt. As regards competition, the sector was very concerned about client poaching, reckless lending by aggressively growing MFIs leading to multiple borrowing, repayment deterioration and over-indebtedness. It was suggested that the community almost unanimously favours the creation of a credit bureau to prevent multiple borrowing and to better assess clients' credit worthiness.

In this paper, **M P Vasimalai and K Narender[20] (2007)**, strongly argues that if micro-credit is not integrated into the larger development perspective there is a danger that it may result in over-indebtedness and financial bondage of the poor. The study was based on the kalanjiam (Tamil word, which means 'prosperity') Community Banking Programme, initiated in 1990, promoted by the DHAN foundation which is unique in terms of the building up demonstrating the viability and sustainability of the SHG-Bank Linkage model. The Centre for Research of DHAN Foundation undertook a study between August 2002 and September 2003. 240 kalanjiam members and 60 respondents from control group were selected through personal interview using structured interview schedule. The study found that the average loan availed from the kalanjiam by a member increased as the membership in the kalanjiam increased. Moreover, the income drains in the form of paying interest at usurious rates to the informal financing system decreased as membership in kalanjiam increased. Around 51 percent (against 81 percent) kalanjiam members could completely repaid their old debts after joining the kalanjiam programme. The kalanjiam unleashed the hidden potential of the members to save. It was reported that there was an increase in family income and improvement in housing condition after intervention of the kalanjiam. The intervention of the Kalanjiam had empowered a considerable proportion of women and led to a change in the gendered roles at the household level. Many of the bankers interviewed had also reported that kalanjiams were regular in repayment. The Kalanjiam programme has demonstrated that even while reaching the poorest of the poor, microfinance operations can be made financially sustainable.

In **(2008) Jayshree Vyas**[21] discussed about the success of SEWA Bank and explained how to approach poor self employed women. She explained that the importance of saving for poor people and MFI because it is a method of ensuring financial discipline which results in improved repayment rates. Banking with poor and mostly illiterate requires special procedure and mechanisms suited to their culture, their needs and their economy.

Kanika Taneja[22] **(2009)** discussed general characteristics of microfinance institutions and gave significant idea about microfinance. She selected Grameen Bank, Bangladesh for her study to explain the financial importance of microfinance as a poverty reduction tool. Grameen bank helped thousands of poor Bangladeshi women to improve their living standard by providing them small loans. By 2003, Grameen Bank had helped between 33-48% of their borrower to move above poverty line. The Grameen Bank has developed a unique financial delivery model which is being widely used in all over the world. The bank achieved up to 95% of loan repayment rate as a result of peer group pressure, and social pressure of being indebted. The Bank also helped their members to get educated by providing educational loans. With the big success in the field of microfinance Grameen Bank has accepted globally in the field of finance as a pioneer of microfinance.

Bharat Bhole, Sean Ogden[23] **(2010)** had compared the presence of strategic default between group lending and individual lending. Secondary data was considered for the purpose of the study. The study found out the results by developing its own statistical model. The paper concluded that unless group members could impose sufficiently strong social sanctions on their strategically defaulting partners, or unless the bank used cross-reporting mechanisms, group lending could perform worse than individual lending. It could yield lower repayment rates, smaller bank profit or smaller borrower welfare. It was showed that when certain restrictions on the group lending contract were relaxed than group lending yields a higher welfare than individual lending even in the absence of any social sanctions or cross-reporting. The study suggested some possible explanation for some of the observed changes in the Grameen Bank of Bangladesh regarding defaults that loan to members should not depend only on group performance but also on her individual performance. The success of microfinance in countries like Bangladesh and Guatemala might be replicated in societies where social connectedness and the ability to impose social sanctions were low.

G. Naga Sridhar[24] **(2010)** discussed that the asset portfolios of microfinance institutions (MFIs) appear to be under stress with increasing reports about the alleged harassments by the recovery agents in the recent past. There are about 2,500 MFIs in the country, out of which only 20 are large. The average interest rate in the industry still remains upward of 28 per cent while it goes over 36 per cent in some cases. During September 2010, names of many big MFIs were linked with such incidents. In Andhra Pradesh alone, 25 persons committed suicide due to harassment from recovery agents/group members, while senior officials of the MFIs had not accepted that. But experts said that the surge in allegations of harassment by recovery agents and fellow-group members are indications of growing non-performing assets in the industry in general.

Anjana Chandramouly[25] **(2010)** has discussed about the critical situations of MFIs during Andhra Pradesh crisis-2010 when MFIs feared rise in customers' defaults. Accordingly banks froze fresh credit line even to those with no exposure in Andhra Pradesh. SIDBI had asked MFIs to draw up a roadmap on reduction of their interest rates. Mr. Ghosh (M.D., Ujjivan Financial Services) pointed out that most banks are in wait-and-watch mode as far as fresh loans are concerned, but there is no pressure on existing loans. Mr. Krishna (M.D., Grameen Koota) added that with banks are freezing the credit lines; our fear is that we might have repayment problems. Other issues that had cropped up include high multiple lending and collection practices, and high return on assets. To counter defaults rising, Microfinance Institutions Network (MFIN), with about 40 members, has planned to come up with a set of standards for pricing, remuneration, return of assets, and return on equity for the industry to avoid Andhra Pradesh like situations.

Suraya Hanim Mokhtar *et al.*[26] (2012) have investigated the determinants of loan repayment problems among microfinance borrowers in TEKUN and YUM institutions in Malaysia. With the aim to empirically analyze the factors affecting the YUM and TEKUN borrowers, 204 TEKUN and 268 YUM borrowers from four states (Selangor, Kedah, Kelantan and Sabah) were selected as a sample using a stratified sampling technique. The primary data were collected through survey interviews using a structured questionnaire. By using logistic regression model, the study showed that the borrower's characteristics (age and gender), business characteristics (business type) and loan characteristics (repayment period, repayment mod and repayment amount) were among the factors that influenced borrowers in repaying their loans. It was suggested that the institutions should guide borrowers to choose the most suitable mode of payment and it must be based on the borrower's revenue cycle. The study showed that lending contract had given problems to borrowers in repaying their loan thus flexibility of the lending contract was really needed in TAKUN and YUM. Overall the findings of the study showed that the loan repayment problems facing the TEKUN and YUM borrowers were not only caused by the individual borrower's characteristics and business type but also the lending system (grace periods, mode of repayment, repayment amount) imposed by the microfinance institutions.

Asif Dowla[27] (2012) has drowned out our attention to how to deal with a default tsunami in the microfinance industry with the example of Grameen Bank, Bangladesh. He revealed that Grameen bank was in serious trouble in 1999. However, the bank and its founder received the 2006 Nobel Peace Prize. This paper discussed about how bank survived the large-scale repayment crisis and near-death experience. Even though the causes of the crises are different, Grameen's experience will be of immense use for MFIs in India. In the first move defaulting members had been classified *viz.* wilful defaulters, destitute defaulters and multiple borrowers, did not pay because they were absent, who left the area permanently and who took large loan by using others as a proxy and due to large debt burden could not repay. The special task force was appointed to rehabilitate troubled bank branches. For the multiple borrowers, the task force made them to sign a contract to repay the principle and interest within a maximum of three years and started issuing new loans equal to the amount repaid in the first six months. The task force also proposed adjusting the group fund against with the bank, even if they had been a member for less than 10 years. Staff members also had been motivated for their monthly work. To install repayment discipline among borrowers, the task force declared to give lucrative leasing loans as reward to borrowers who deposited savings, attended meetings regularly and had perfect repayment records. Grameen Pension, Savings and Insurance program were also been introduced for borrowers to reconnect them with the bank. For wilful defaulters, the task force started issuing legal notice against them and that technique worked. At the end of December 2000, bank's condition was found improved and the bank codified into Grameen II. In the new model the loan can be repaid over three months or three years instead of 52 weeks. Instead of whole group, only borrower is liable for repayment of the loan. Borrowers facing repayment difficulties can switch to a flexible loan that extends the time of repayment and reduce the amount of instalment payments. The study suggested that MFIs have to develop organizations that can respond to changes in the market, build a culture of openness that encourages problem-solving, employ an MIS and accounting system that can identify excessive lending, develop human resources with diversified skills, and expand at a rate that is commensurate with the needs of the borrower, and use other metrics of success in addition to the repayment rate.

K. Raja Reddy *et.al*[28] (n. d.) examined the loan default and recovery in SHG-Bank Linkage Programme. The study looked at the issues of default in SHGs (Self Help Groups), factors contributing to it and various mechanisms to address defaults and recoveries. The data of 42 default SHGs from six bank branches in four mandals in three revenue divisions were collected by conducting personal interview and focused on group discussion from PSR Nellore district of Andhra Pradesh during 11th to 14th October 2010. It was observed that defaults in SHGs declines the functional as well as financial aspects of a group over a period. The study also focused on to understand to what extent the SHGs and their members borrowed multiple and large volume of loans from village organizations (VOs), banks and commercial microfinance institutions (MFIs). It was found that average loan size of MFIs is higher than the loans taken from other credit sources. Over loaning of SHGs by multiple sources also leads to default. The study reported the two types of reasons for default such as genuine defaulting and wilful defaulting. Genuine was because of poverty, vulnerability and risks which included an accident, illness or death in the family, crop failure etc. Wilful was related to lack of discipline in the group. The lending norms, the shortcuts in practice in order to achieve both stated and unstated ends of banks, MFIs and groups; vested interest of the political parties; poor implementation of polices; and poor systems and institutions have been significantly contributed to defaulting. It was concluded that whether it was a bank or MFI, responsible lending would alone optimize development and minimize risks of SHGs.

The studies related to social aspects revealed that micro financing can improve health, sanitation, education and living standard of the poor people. By focusing specially on women, it was observed that microfinance create social capital where their level of consciousness, awareness and decision making abilities can be improved. The studies related to financial aspects reveals that poor people are also bankable and good repayers of loans. Credit facilities given through group methods can generate good repayment record. Microfinance can increase level of income, assets, savings and borrowers capacity of the poor people through which their financial status can be improved. However, sometimes poor people defaults due to some unavoidable reasons such as sickness, unemployment, social customs, sudden expenses, delay in repayment of wages etc. But the repayment rates can be controlled with close monitoring, more staff, better internal financial and management discipline, and changing lending system according to the need of poor etc.

2.2 Reviews from Foreign Authors

Some foreign authors also shared their views regarding the area of microfinance. Some reviews found important for the purpose of the study which are included here.

2.2.1 Social Aspects

Lia CH Fernald *et al.*[29] (2008) focused on the effects of microcredit on levels of perceived stress and psychological functioning of participants. Microcredit programmes might improve the economic conditions of clients. It also improved lives of participants in social and health domains as well. Increased income through microcredit improves health outcomes (physical and mental) in the primary pathway. But on the other hand incurring loan debt could certainly increase financial strain and psychological stress for some poor families, especially if they struggle with repayment. Sample frame (257) was comprised of individuals (women and men) all from separate households who had applied to an individual lending organization with branches in Cape Town, Port Elizabeth, and Durban in South Africa. After analyzing the data with regression the findings suggested that one mechanism used to reduce the economic stress of extremely poor individuals could have mixed effects on their levels of psychological stress and symptomatology. The data also suggested that randomization into receiving a second chance for a small individual loan was associated with increased levels of perceived stress among the general sample, with important differences by gender. Men might benefit more than women from cash loans because they were better able to take advantage of cash alone whereas women might need the support of the group lending mechanism. The differential effects for men and women found should also be investigated further including assessments of economic resources and psychological function at baseline.

Samuel Adams[30] **(2010)** has observed the impact of microfinance from the perspectives of maize farmers in Nkoranza in the Brong Ahafo Region of Ghana. Primary data was obtained from interviews and group discussion and secondary data obtained from Agricultural Development Bank (ADB), the managers of the Ghana government's Food Crop Development Project (FCDP). With the analysis of the data of 100 beneficiaries of the FCDP and 100 saving account holders at ADB, the study found out that microcredit positively affects on the education of beneficiaries' children, health care, housing, clothing and community obligations. Findings of the study had suggested that microfinance had a marginal effect on both the economic and social wellbeing of the recipients of the credit facility. But the discussion also showed that only microfinance is not enough to alleviate poverty. The lake of infrastructure and market for products contributed to the inability of most of the recipients to pay off their debt. Since all the recipients had other jobs apart from maize production, it means that the rural non-farm sector needs to be developed. It was suggested that microfinance could play a huge role in alleviating poverty if it helps to find ways through the market to get new opportunities to earn income by the investments in both farm and non-farm activities. There was the need to examine how, when, and what type of linkages between the non-farm and farm sectors were needed to give the desired effect on productivity.

Group lending is said to be the key factor in microfinance by mitigating information problem and therewith increasing repayment rates. In recent years, however, individual loans have also been given to the poor in developing countries. But **Helke Waelde**[31] **(2011)** questioned that which type of loan would be the best for the borrower. With the reviews of past literature, a loan market is modelled where individual and group loans exist side by side. The study enriched standard economic analysis by social component, the social prestige function with an externality. When individual lending has been compared with group lending, group lending consisted of three additional mechanisms: the fee for joining a group, a payment in case her project fails and the social prestige function. The study looked at the model with no externality and with a negative externality. In general it was found out that there is too much group lending in microfinance. If there was no externality, borrowers should borrow individually only. If there was a negative externality, entrepreneurs should start with group lending if they were very poor. If a borrower possessed more than a critical level of wealth, it was optimal for her to switch to individual borrowing. The study provided an initial theoretical explanation for the gradual replacement of group loans by individual loans in microfinance as it is being shown in developing countries today. The study suggested to support individual lending in development policy as opposed to group lending in order to increase borrower's expected utility and the welfare of the economy as a whole.

2.2.2 Financial Aspects

Monika Huppi, Gershon Feder[32] (1990) carried out the review of literature and assessed factors affecting the success of rural lending groups and cooperatives. The study revealed the success of group lending ventures as follows: the homogeneous groups that were jointly liable assumed some managerial and supervisory responsibility to repay but mandatory joint liability was effective only if borrowers had strong reason to believe that their peers would also repay; in case of default made by any borrower from the group, all group member would not access future credit. However, this threat would work only as long as the lender was able to provide favourable and timely credit services in the future. The success of group lending also depend upon previous experience with group activities and a common bond other than credit. The study found important factors in the success of credit cooperatives include: bottom-up institutional development and training at the grass-roots and management levels, reliance on members' deposits rather than on outside sources for funds, the limiting of activities to financial intermediation (unless strong institutional and management capabilities exist).

Joseph E. Stiglitz[33] (1990) focused on the effects of peer monitoring in the credit market. Peer monitoring was largely responsible for the successful financial performance of the Grameen Bank of Bangladesh. The study was based on the secondary data. Different views questioned on exploitation and suggested that high rates were a result of three factors: the high rates of default, the high correlations among defaults and the high cost of screening loan applicants and pursuing delinquent borrowers. The study analyzed that peer monitoring decrease the rate of defaults because the group acts like a cooperative, if some individual was more prone to default than others, he was being subsidized. This article has illustrated in a simple way by which such peer monitoring could be implemented, but there were alternative institutional arrangements that could work as well or better. The government could lend to small lending cooperatives within a village, making each member of the cooperative collectively liable for the whole. The members of the group must be provided with incentives to monitor the actions of their peers.

Timothy Besley, Stephen Coate[34] **(1995)** presented the paper with the aim to understand the impact of two important features *i.e.* joint liability and social collateral on repayment decisions in group lending. Author had developed different models for group lending and individual lending to investigate repayment incentives. The model gave following results: if the group was formed from communities with a high degree of social connectedness, then this might constitute a powerful incentive device and hence might serve to mitigate any negative effects from group lending. If social penalties were severe enough, group lending would result in a higher repayment rate than individual lending but it should not be taken as implying that group lending was better or worse than individual lending in any broader sense than repayment rates.

Imran Matin[35] **(1997)** provided further evidence of repayment problems in group credit program of Grameen Bank borrowers using survey data collected during 1994-95 in four villages of Madhupur, Thana in Bangladesh because the area seemed to have worsened repayment problems in 1995. The researcher collected household and individual level information on 246 Grameen Bank borrowers in the study area who had an outstanding loan according to the 1995 year end statement. Besides using a formal econometric model to delineate the factors associated with loan repayment behaviour of borrowers, the study suggested the followings: the education status of the household has strong negative effect on default status irrespective of the household's income position, the total operated landholding of the household was negatively associated with default status of the borrowing household but was positively associated with default after a certain level, membership period affected positively because it build the optimum level of trust between the borrowers and the bank, intensity of the NGO participation of the borrowing household affects default probability positively, NGO competition be managed and monitored in ways that do not impair each other's repayment performance. Another most important finding was that the group collateral approach seems to be most effective when loan sizes were relatively small.

Manfred Zeller[36] **(1998)** discussed about to investigate the effects of intragroup pooling of risky assets or projects by controlling for community level and program design factors that influence the repayment rate of group loans. Random sample of 146 groups from six different lending programs in Madagascar (Implemented in four agro ecological regions) were selected for the study during 1992. Primary data was collected by interviewing randomly selected presidents of each group. The survey comprised three units of observation: households, credit groups and communities. The model was estimated by using the TOBIT maximum likelihood technique. The study finally revealed that Groups, located in communities with a high exposure to covariate risks, had a significantly lower repayment rate than those with lower exposure. In order to cover the costs of expected higher loan default in risk-prone communities, programs could charge higher interest rates or set up member financed credit guarantee funds, which could be used to cover loan defaults. The diversification of the joint assets and enterprise portfolio among members of the same group and related risk pooling and social cohesion among members could augment the repayment performance in group-lending schemes.

Martha Alter Chen and Donald Sondgrass[37] (1999) had presented a working paper of a baseline survey (January-March 1998) of 900 low-income working women engaged in own-account, sub-contracting and labour activities in Ahmedabad, India. The purpose of the survey was to provide preliminary indications of the nature and magnitude of benefits resulting from participation of the microenterprise services of SEWA bank. In keeping with the framework of the Assessing the Impact of Microenterprise Services (AIMS) project, three groups of 300 respondents each were compared *viz.* current borrower from SEWA bank; savers in the bank who were not current borrowers; and a control group of non-members of SEWA. Numbers of hypothesis about possible impacts at the household, enterprise and individual levels were tested (AIMS core team 1997). These hypotheses carried out in Lima, Peru and Zimbabwe. After using basic statistical tools *viz.* frequency, percentage, mean, median, the study found the following. Household level survey concluded that participation in microenterprise services made many positive changes in members of SEWA bank as compared to the control group. Enterprise level survey informed that SEWA credit might raise the revenue earned by the borrower's own principal own account activity. Savings might increase revenues from sub-contracting activity when that is the borrower's principal economic activity. The study could not find enough evidence that participation in microenterprise services leads to increase in enterprise fixed assets. In summary, enterprise level impacts were not very strongly supported by the survey results. Individual level hypotheses pointed out that participation in microenterprise services leads to an increase in the client's control over resources and income within the household economic portfolio. It also increased self-esteem and self-confidence among the borrowers over savers and control group. Ability to deal with the future was also higher among the borrowers over the savers and control group. As SEWA bank helps its members to pay off outstanding non-SEWA debts, participation also leads to decrease in indebtedness among SEWA members. Though impacts of the SEWA bank are positive, further research would be needed.

Jean-Jacques Laffont, Tchetche N'Guessan[38] **(2000)** focused on group lending with adverse selection of group members and examined its effect on repayment rate. The author defined two different models; for good type of borrowers *i.e.* have sure projects with return and bad types of borrowers *i.e.* have projects with zero return. The model concluded that when borrowers know each other, group lending contracts were useful even if collusion with side contracts took place. But now the optimal collusion proof group contract did better than individual contracts, but it was not efficient. If borrowers were adversely selected there was no collateral effect due to grouping.

Gwendolyn Alexander Tedeschi[39] **(2006)** presented a model of microfinance lending to individuals to show how dynamic incentives, in the form of additional loans, could reduce strategic default without relying on the group incentives. The model had been created to define the relationship between lender and borrower in two different phases: lending phase (one loan is successfully repaid, another loan is given) and punishment phase (the borrower defaults, no new loans are given). The paper showed that MFIs attempts to improve and expand upon savings and insurance products. If borrowers could be sheltered from the unplanned expenditures or loss of income, or be better able to cope with economic loss when it occurs, their ability to repay would be higher, and thus default would be lower.

Niels Hermes and Robert Lensink[40] **(2007)** collected literature on microfinance and found out various reasons regarding the repayment performance of joint liability group. There had been empirical evidence that repayment performance of group improved when groups had written (formal) rules stating how members should behave. Groups located in remote areas could reduce their possibilities for access to alternative sources of credit which stimulates them to ensure group repayment as much as possible in order to have future access to loans. Other important evidence showed that repayment problems increase when there were more relatives in the same group as screening, monitoring and enforcement among relatives did not take place and relatives might easily collude against the programme and delay repayment. Groups with stronger social ties showed higher repayment rates. Groups with internal rules and regulations also demonstrated better repayment rates. It was also noticed that average distance between group members negatively influence repayment performance. The quality of the group leader in running group positively affected on group repayment performance. There was evidence that the homogeneity of the group in terms of their ethnicity, occupation, income etc. reduced their repayment performance because they had lower incentives to screen, monitors, and enforce each other and/or might start to collude against the programme.

Thi Thu Tra Pham and Robert Lensink[41] **(2007)** presented comparative study between lending policies of formal, informal and semiformal lenders with respect to household lending in Vietnam. The data were drawn from household survey standards in Vietnam, the Vietnam Living Standard Survey (VLSS). That survey was conducted by Vietnam's General Statistical Office in 1998, with financial assistance from the United Nations Development Programme (UNDP) and the Swedish International Development Agency (SIDA), and technical assistance from the World Bank. The survey covered a sample of 6,002 households from which 4,334 observations were selected from formal, informal and semiformal financial intermediaries and 111 observations were selected from unclassifiable sources. By using regression analysis the study observed that a household capable of providing collateral and/or finding a guarantor was more likely to use formal and semiformal credit. Low income households and or female borrowers had preferred informal credit. Analysis of some determinants of probability of default showed that there were some contract and borrower characteristics that are important for one type of creditor but not for the others. Formal credit institutions tend to associate the probability of default with contract-related items such as the loan interest rate and the form of loan repayment. Informal lenders, on the contrary, tend to link default risk to household-related characteristics and especially the presence of close lender–borrower relationships. Semiformal creditors perform as the combined form of the other groups, given the application of certain contracting tools and the reliance on borrower characteristics for managing risk. It was recommended to lenders of all sorts to exert tighter monitoring over such loans.

Erica Field and Rohini Pande[42] **(2008)** collected data from a field experiment, between April to September 2006, from a leading MFI 'Village welfare Society', Kolkata to examine whether repayment frequency affects loan default and delinquency on first-time borrowers. The experiment formed one hundred groups consisting of 1026 first time borrowers while group size ranged from 8 to 13 members. Least square regression method was used for testing statistically significant differences in repayment behaviour between the experimental arms: (a) weekly repayment schedule at weekly meetings, (b) monthly repayment schedule at monthly meeting and (c) a monthly repayment schedule at weekly meetings which required to attend weekly meeting for the first three months after loan disbursement, after which point borrowers had been graduated to a monthly meeting schedule. The study found the following: switching from weekly to monthly instalments did not affect client repayment capacity while most of microfinance practitioners believe that more frequent repayment schedules improve client repayment rates. The result suggested that switching to lower frequency repayment schedules could allow MFIs operating in comparable settings to save dramatically on the transaction costs of instalment collection facing virtually no added risk of default. No evidence to prove that lower frequency repayment schedules encourage irresponsible repayment behaviour among first-time borrowers receiving small loans. As instalments were collected in group meeting it is suggested that less frequent repayment schedules did not increase per meeting transaction cost of collection.

Erica Field, Rohini Pande, John Papp[43] (2009) had analyzed the effect of repayment flexibility on entrepreneurial behaviour and loan default. The study was focused on a central feature of the classic "Grameen Bank" contract: repayment in small instalments starting immediately after loan disbursement. The study provided rigorous evidence that both client investment and repayment behaviour was sensitive to when repayment obligations start. The study was based on primary data collected from the MFI, "Village Welfare Society" (VWS), in the West Bengal. The secondary data was collected from VWS officers. Total 845 clients were selected as a sample. The baseline surveying was conducted between April and August 2007 and endline surveying between January and November 2008. The study found out that average level of default and delinquency rise when clients were offered a grace period before repayment begins while delayed repayment encourages more profitable, though riskier investment. The study found 3% default rate for clients without a grace period and 11% default rate for the clients with a grace period. It was suggested that VWS would have to increase its annual interest rate (from 22% to 33%) to cover the additional default. Of course, the higher interest rate might itself cause a yet higher default rate if moral hazard or adverse selection were significant, so the new interest rate should have been taken as a minimum.

Jessica Schicks[44] (2012) had worked with a unique dataset from a survey among micro borrowers in Accra, Ghana. In cooperation with the Independent Evaluation Department of the German development bank KfW and with the Smart Campaign hosted by ACCION International, 531 structured interviews were conducted among microfinance borrowers at the end of 2010. Logistic regression analysis was used to identify how poverty, adverse shocks, loan returns and financial literacy relate to over-indebtedness. The study concluded that micro borrowers were more likely to be over-indebted when they were living on lower incomes and lower assets. MFIs might be able to reduce over-indebtedness by reducing credit to poorer borrowers, lending smaller amounts, or choosing to not lend to the poorest borrowers. Adverse shocks to income and expenses represented a main cause of over-indebtedness among borrowers. MFIs should anticipate the occurrence of adverse shocks when determining creditworthiness and deciding on loan amounts and instalment schedules. The paper identified that non-productive loan use increases the risk of over-indebtedness. Low return on invested loans was related to higher over-indebtedness risks. It was showed that borrowers were more likely to be over-indebted when they lack financial literacy to understand debt products. General financial literacy seems to have an opposite effect, contradicting researcher's expectations. It was suggested that improving borrowers' financial literacy could reduce their risk of over-indebtedness. For mere numeracy, there was no statistically significant effect on over-indebtedness.

2.3 Summing Up

Various financial facilities provided by MFIs helps poor people to grow but recovery of collateral free loans is a very big concern for MFIs. Group lending was found very significant delivery channel in the field of microfinance. Group lending helps poor people to improve their social as well as financial status. Group lending also works as group collateral because in group lending all group members are jointly liable for the group loan so peer pressure was found to be the most effective tool from the point of view of repayment. However, individual lending was also found important because peer pressure do not work positively all the time. Some evidences were found that because of peer pressure some group dissolved and members started borrowing on individual level. Some common reasons found for loan defaults in individual lending were sickness, death in family, social customs, delay in payment of wages, anti-social influence, unemployment, and sometimes unwillingness to repay. Solutions to decrease default level found are as follows: Personal and continuous contacts of the members, close monitoring, understand the needs of the poor, providing proper knowledge to the poor and providing many supportive services over and above credit etc. Close coordination between members and organizers help MFIs to maintain the low level of defaults and also help members not to be trapped into indebtedness.

☆☆☆☆☆

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